



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
TEGE EO Examinations Mail Stop 4920 DAL
1100 Commerce St.
Dallas, Texas 75242

501.03-00

Date: July 30, 2012

Release Number: 201245025

Release Date: 11/9/2012

LEGEND

ORG – Organization name

XX – Date Address – address

Taxpayer Identification Number:

Person to Contact:

Employee Identification Number:

Employee Telephone Number:

(Phone)

(Fax)

ORG

ADDRESS

CERTIFIED MAIL – RETURN RECEIPT

Dear

This is a final adverse determination regarding your exempt status under section 501(c)(3) of the Internal Revenue Code. Our favorable determination letter to you dated May 20XX is hereby revoked and you are no longer exempt under section 501(a) of the Code effective January 1, 20XX.

The revocation of your exempt status was made for the following reason(s):

Organizations described in IRC 501(c)(3) and exempt under section 501(a) must be both organized and operated exclusively for exempt purposes. You have failed to establish that you are operated exclusively for exempt purposes and that no part of your net earnings inures to the benefit of private shareholders or individuals. A substantial part of your earnings inure to the benefit of your members. A substantial part of your activities do not further an exempt purpose.

Contributions to your organization are no longer deductible under IRC §170 after January 1, 20XX.

You are required to file income tax returns on Form 1120. These returns should be filed with the appropriate Service Center for the tax year ending December 31, 20XX, and for all tax years thereafter in accordance with the instructions of the return.

Processing of income tax returns and assessments of any taxes due will not be delayed should a petition for declaratory judgment be filed under section 7428 of the Internal Revenue Code.

If you decide to contest this determination under the declaratory judgment provisions of section 7428 of the Code, a petition to the United States Tax Court, the United States Claims Court, or the district court of the United States for the District of Columbia must be filed before the 91st Day after the date this determination was mailed to you. Please contact the clerk of the appropriate court for rules regarding filing petitions for declaratory judgments by referring to the enclosed Publication 892. You may write to the United States Tax Court at the following address:

You also have the right to contact the Office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal Appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free, 1-877-777-4778, and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

Nanette M. Downing
Director, EO Examinations

Internal Revenue Service

Department of the Treasury

Internal Revenue Service

TE/GE: EO Exam

1100 Commerce Street

Dallas, TX 75242

Taxpayer Identification Number:

Date: June 1, 2012

Form:

ORG

Tax Year(s) Ended:

ADDRESS

Person to Contact/ID Number:

Contact Numbers:

Telephone:

Fax:

Certified Mail - Return Receipt Requested

Dear

We have enclosed a copy of our report of examination explaining why we believe revocation of your exempt status under section 501(c)(3) of the Internal Revenue Code (Code) is necessary.

If you accept our findings, take no further action. We will issue a final revocation letter.

If you do not agree with our proposed revocation, you must submit to us a written request for Appeals Office consideration within 30 days from the date of this letter to protest our decision. Your protest should include a statement of the facts, the applicable law, and arguments in support of your position.

An Appeals officer will review your case. The Appeals office is independent of the Director, EO Examinations. The Appeals Office resolves most disputes informally and promptly. The enclosed Publication 3498, *The Examination Process*, and Publication 892, *Exempt Organizations Appeal Procedures for Unagreed Issues*, explain how to appeal an Internal Revenue Service (IRS) decision. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process.

You may also request that we refer this matter for technical advice as explained in Publication 892. If we issue a determination letter to you based on technical advice, no further administrative appeal is available to you within the IRS regarding the issue that was the subject of the technical advice.

If we do not hear from you within 30 days from the date of this letter, we will process your case based on the recommendations shown in the report of examination. If you do not protest this proposed determination within 30 days from the date of this letter, the IRS will consider it to be a failure to exhaust your available administrative remedies. Section 7428(b)(2) of the Code provides, in part: "A declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the Claims Court, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted its administrative remedies within the Internal Revenue Service." We will then issue a final revocation letter. We will also notify the appropriate state officials of the revocation in accordance with section 6104(c) of the Code.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free 1-877-777-4778 and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter. If you write, please provide a telephone number and the most convenient time to call if we need to contact you.

Thank you for your cooperation.

Sincerely,

Nanette M. Downing
Director, EO Examinations

Enclosures:
Publication 892
Publication 3498
Report of Examination

Form 886-A (Rev. January 1994)	EXPLANATIONS OF ITEMS	Schedule number or exhibit
Name of taxpayer ORG	Tax Identification Number EIN	Year/Period ended 12/31/20XX 12/31/20XX

LEGEND

ORG - Organization name XX - Date City - city County - county State - state
CO-1 through CO-16 - 1st through 16th COMPANIES

Issue

Whether the ORG is still exempt under Internal Revenue Code (IRC) section 501(c)(3).

Facts

Articles of Incorporation

The ORG (hereinafter referred to as "organization" or "ORG") is a State non-profit public benefit organization. ORG's Articles of Incorporation state it was formed to promote competitive amateur athletic teams from County in state, regional and national competition within the meaning of 501(c)(3) of the IRC. The Articles also provide that no part of its net income or assets will inure to the benefit of any director, officer, or member.

Form 1023: Application for Recognition of Exemption

In its "Application for Recognition of Exemption," the organization states its purpose is to:

- "Support national and international amateur athletic cheerleading competition", through
- Raising public and private support for cheerleading teams to attend national and international competitions.
- Hosting public demonstrations to raise awareness of cheerleading as an athletic discipline.
- Hosting cheerleading training clinics for beginning and advance cheerleaders.

The organization stated that its main source of income would be from donations by public corporations and private individuals, membership dues and fundraising events.

It fundraising program will consist of "fundraising activities at public athletic venues in which corporate sponsors make contributions to participating non-profit organizations."

Determination Letter

The organization received its exemption letter in May of 20XX, effective March 27, 20XX. During its advance ruling period, the organization was determined to be exempt from federal income tax under 501(a) of IRC as described in section 501(c)(3). The organization was further classified to be a publicly supported organization described in sections 509(a)(1) and 170(b)(1)(A)(vi) of the IRC.

Correspondence received September 15, 20XX stated the organization is classified as a 509(a)(2).

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Bylaws

The ORG's amended its Bylaws in 20XX. Its objective and purpose is to promote and support curricular and athletic achievements for people of all ages.

The organization is a membership organization. The amended bylaws state membership qualifications as follows:

The qualifications for membership in this corporation are to be a person or corporation interested in promoting and supporting curricular and athletic achievements. Personal and corporate members shall each pay the dues prescribed by the Board of Directors. Further, personal members shall commit to those hours of volunteer service, or payment of a contribution in lieu of volunteer service, as the Board of Directors may determine.

Membership

In the tax years under audit, 20XX and 20XX, the organization had 70 members. Membership is made up of primarily parents of student athletes.

The membership packet for the May 1, 20XX through April 31, 20XX season includes a welcome letter from the President; venue, dress code & rules; what to expect & distribution of funds; educational expense requests; request for transfer form; and membership plans.

The welcome letter in the membership packets states the following:

Although we do not claim to cover your entire cost of extra expenses, we do feel that becoming an active member of the ORG will allow you to accumulate tax free funds to help defray your expenses.

The organization list eight venues it volunteers at CO-1/CO-2/CO-3 & CO-4, CO-5 "CO-6", CO-7 & CO-8, and CO-9.

The organization requires tuition request, private and extra classes with CO-10 to be submitted by the 20th of each month. Requests made after the 20th will be used for the next month's tuition or payment.

Educational expense payments are made directly to an accredited school. Requests can be made for room and board, board deposits, tuition and extended expenses. To receive tuition request payments, the individual must be an active and current member of the organization. The transfer request must be submitted by the submission date. The individual must have balance availability and have the original or photo copy receipt from school.

Activities

Sports Venues

Form 886-A (Rev. January 1994)	EXPLANATIONS OF ITEMS		Schedule number or exhibit
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The organization's main activity is volunteering at sporting events to work in concession stands. The organization supplies the workers, and the concession company supplies the inventory and supplies needed in the stand. Once a member joins the organization and pays their membership dues, they are invited to join the organization's e-group, which is used to post and sign up for events.

Two contracts the organization worked at in 20XX and 20XX were provided. The first contract with the CO-5 in City covers the period of September 10, 20XX to July 31, 20XX. The contract states that in exchange for the conduct of the concession operations, the organization will receive a percentage of the total gross receipts from the concession operations determined by a pay per person scale. The second contract is with CO-11 in City entered into on March 15, 20XX. The contract states that in exchange for supplying volunteers to work and sell concessions, the organization will receive 12% of profits earned. All volunteers must sign an acknowledgement and release form before performing any services.

In 20XX, the organization worked at eight event venues and earned a total of \$ for work performed at approximately 121 events.

CO-5
CO-2
CO-11
CO-12
CO-13
CO-14
CO-15
CO-16

Total

Scholarships

The organization's second activity in conjunction with its fundraising is granting "scholarships" to members' children for cost of tuition, books, etc. from the monies received from the fundraising venues. Each member is granted a scholarship based on the amount he or she contributes to the organization through fundraising at the sporting events. The members' scholarship amount is determined based on the funds he or she raises. The amount requested cannot exceed the amount in the members' account. To request a scholarship, each member must submit a "Request for Transfer" form along with receipts for the amount requested. The details requested on the form includes the member's name, date of the request, child's name, program/group, amount, and payee name for the check.

Scholarships are distributed based on membership status and the number of fundraising events attended. Provided the members participated in volunteering events, and does not request more than he/she has contributed, the request will be granted. A check would then be written by the Treasurer and issued to the School, CO-11, or parent based on the details of the request.

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A sample of the organization's Request for Transfer Forms in 20XX and 20XX show that all payments made to academic institutions or CO-10 were earmarked for a specific member child's tuition or for reimbursement directly to the member for a child's cost of college books, travel, or apparel. The members submitted a request for transfer form which included the member's name, child's name, program, amount requested, name the check should be written and reason for the request.

In 20XX and 20XX, the organization granted \$ and \$ in scholarships to members' children. This was the organization's primary expense in both years under audit.

The President provided a statement in response to information document request #1 that "it is the understanding of organization that all participants in each program or school athletic program that receives the requested monies will benefit from the members request."

In reply to information document request # 2, the organization stated that no public scholarships were given in 20XX due to lack of surplus. There were no records of public scholarships distributed before 20XX, when there was a surplus. In 20XX a committee of two board members and two general members was formed. Scholarship applicants submitted two essays and a recommendation letter. Each essay and letter was independently graded and ranked. All applications (13) received scholarships; the amounts were determined by ranking.

Law

IRC section 501(c)(3) provides that organizations organized and operated exclusively for charitable, education, religious, scientific, testing for public safety, literary or to foster national or international sports, or the prevention of cruelty to children or animals is exempt. The code section also requires that there be no inurement of earnings to private shareholders or individuals.

Treas. Reg. section 1.501(c)(3)-1(c)(1) states that an organization is operated exclusively for exempt purposes if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3). It goes on to say that an organization will not be regarded as operating exclusively for exempt purposes if more than an insubstantial part of its activities is for a non-exempt purpose. The presence of a single substantial nonexempt purpose destroys the exemption regardless of the number or importance of the exempt purposes. *Better Business Bureau v. United States*, 326 U.S. 279, 283, 90 L. Ed. 67, 66 S.Ct. 112 (1945); *American Campaign Academy v. Commissioner*, 92 T.C. 1053, 1065 (1989).

Treas. Reg. section 1.501(c)(3)-1(c)(2) states that an organization is not operated exclusively for one or more exempt purposes if its net earnings inure in whole or in part to the benefit of private shareholders or individuals. Treas. Reg. section 1.501(a)-1(c) defines private shareholder or individual as persons having a personal and private interest in the activities of the organization.

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Treas. Reg. section 1.501(c)(3)-1(d)(ii) provides that an organization is not organized or operated for purposes of Section 501(c)(3) if it serves a private rather than public interest. To meet this requirement it is necessary for an organization to establish that it is not organized or operated for the benefit of private interests such as designated individuals, the creator or his family, shareholders of the organization or persons controlled, directly or indirectly, by such private interests.

In determining the effective date of revocation, an organization may ordinarily rely on a favorable determination letter received from the Internal Revenue Service. Treas. Reg. §1.501(a)-1(a)(2); Rev. Proc. 20XX-4, §14.01 (cross-referencing §13.01 et seq.), 20XX-1 C.B. 123. An organization may not rely on a favorable determination letter, however, if the organization omitted or misstated a material fact in its application or in supporting documents. In addition, an organization may not rely on a favorable determination if there is a material change, inconsistent with exemption, in the organization's character, purposes, or methods of operation after the determination letter is issued. Rev. Proc. 20XX-52, 20XX-30, IRB 222.

The Commissioner may revoke a favorable determination letter for good cause. Treas. Reg. § 1.501(a)-1(a)(2). Revocation of a determination letter may be retroactive if the organization omitted or misstated a material fact or operated in a manner materially different from that originally represented. Rev. Proc. 20XX-52, 20XX-30 IRB 222.

Taxpayer's Position

In discussion with the taxpayer's representative on March 28, 20XX, the representative agrees to the revocation.

Government's Position

The ORG is not operated exclusively for exempt purposes. Its earnings inure to the benefit of its members who participate in fundraising. More than an insubstantial part of its activities is in furtherance of a nonexempt purpose of reducing costs to members.

The ORG earnings inure to the benefit of its members. The members receive a direct benefit in proportion to their participation at fundraising events. The ORG requires members to submit a request for transfer for all payments. Requests show amounts paid to each institution are earmarked for a specific child's athletic or academic tuition fees. The payments benefit the individual child rather than the institution as a whole. As a result, the ORG's activities result in the inurement of its income to its members.

The ORG's Bylaws state that the organization is to promote and support curricular and athletic achievements for people of all ages. However, the system in place does not benefit the public as a whole; instead it benefits the individual member and their children.

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The organization's only activity is operating a concession stand at sporting venues to fundraise for members. Fundraising in itself is not generally a charitable activity. Fundraising is a means for an organization to raise income for use in its charitable or educational programs. An organization that is created to raise funds to donate to another charitable organization may have fundraising as its only activity. For example, an organization set up to raise money to support the local library. This type of organization is exempt because all income raised is donated to the local library. Unlike the present case, in which the income earned is earmarked for members and their children's educational or athletic fees.

The ORG's purpose is to raise funds for members. This is not an exempt activity. An organization does not qualify to be exempt if more than an insubstantial part of its activities is for a nonexempt purpose. In the case of the ORG, 100% of its activities are for a nonexempt purpose. Therefore, the organization does not qualify to be exempt under section 501(c)(3) of the IRC.

Effective Date of Revocation

While revocation of a determination letter is generally not retroactive, revocation of a determination letter may be retroactive if the organization omitted or misstated a material fact or operated in a manner materially different from that originally represented. In cases where the organization omitted or misstated a material fact, revocation may be retroactive to all open years under the statute. In cases where revocation is due to a material change, inconsistent with exempt status, in the character, the purpose, or the method of operation, revocation will ordinarily take effect as of the date of the material change. In any event, revocation will ordinarily take effect no later than the time at which the organization received written notice that its exemption ruling or determination letter might be revoked. Rev. Proc. 20XX-52, 20XX-30 IRB 222.

In this case, the agent recommends retroactive revocation of the determination letter because the organization operated in a manner inconsistent with its exempt status under IRC 501(c)(3). Therefore, it is recommended that revocation be effective as of January 1, 20XX.

Conclusion

The exempt status of the ORG should be revoked because a substantial part of its earnings inure to the benefit of its members and a substantial part of its activities do not further an exempt purpose.

The agent recommends retroactive revocation of the determination letter because the organization operated in a manner inconsistent with its exempt status under IRC 501(c)(3). Therefore, it is recommended that revocation be effective as of January 1, 20XX.